

France Market in Minutes

A stifled market that continues to appeal to investors

Q4 2016

Financial markets look to property investment

■ According to the latest IMF forecasts, global economic growth in 2016 should follow in the footsteps of 2015, standing at +3.4%. 2016 saw France benefit from slightly stronger GDP growth (+1.3% compared to 1.1% in 2015), along with a fall in trend in unemployment rates (9.7% at the end of 2016).

■ Despite troubling factors such as the volatility of oil prices, fears of a slowdown in China, the Brexit vote and more recently, Donald Trump's election as President of the United States, financial markets have remained optimistic and any volatility has proven short-lived.

■ This is proof of the finance sector's confidence in the supportive policies being implemented by central banks, which have kept interest rates at historically low levels, allowing markets to enjoy record levels of liquidity.

■ The moderate rise in long-term rates (10-year OAT government bonds at 0.68% at year-end) poses no risk to commercial property investment strategies, with good financial terms and conditions available thanks to a spread of over 200 bp.

One of the best investment volumes since the onset of the crisis

■ This high liquidity has generated strong demand, and as a result nearly €27.5 billion worth of capital flowed into investment markets in 2016. This represents yet another yearly increase (+3%) and marks a new high since 2007, thanks to an increase in the number

of deals over €500 million (6 in total, of which 2 were for over €1 billion).

■ Moreover, the amendment to the France-Luxembourg Agreement, which sees capital gains in France being taxed as of January 2017, unleashed a slue of early sales of assets held by Luxembourg-based funds. These deals have slightly inflated market figures.

■ The level of investment over recent years has remained high, but could improve even further as the amounts available are significant and rising year-on-year. This is the case for French property funds (SCPI), generating increasing levels of return.

Lack of supply in the face of growing demand

■ In 2016, growing demand for Core assets, particularly offices, highlighted the supply-demand imbalance and further hardened yields. The prime office

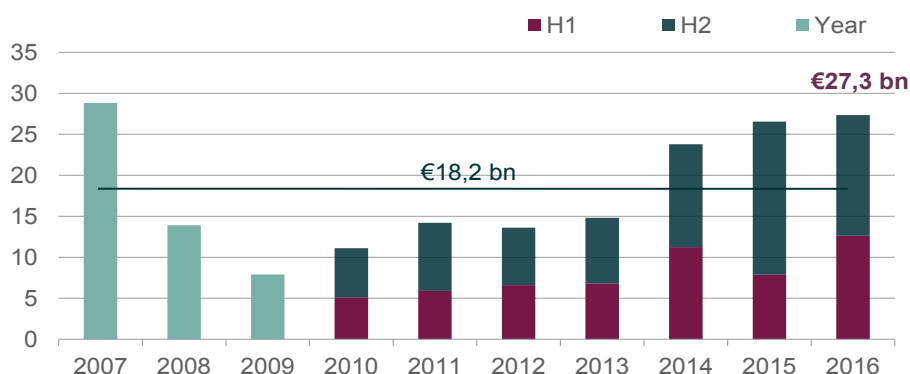
yield fell further before levelling out at 3% by mid-year.

■ The lack of available secure assets is forcing a change in fund strategies. In the search for improved returns, long-term investors are taking on greater rental risk and/or shifting their attention to periphery markets. The increase in forward funding developments (VEFA) is one example of this. With investors widening their radar, new tensions are appearing in the value-added assets market.

■ Asset diversification has also rippled out to alternative investment products. Their market share increased from 7% in 2015 to 14% in 2016. This niche market is renowned for its portfolios and forward funding developments properties: among others, Eurazeo acquired a portfolio of 85 hotels for €504 million and Primonial Reim acquired a portfolio of 26 healthcare assets for €301 million.

GRAPH 1

Investment annual change The abundance of liquidity is pushing up investment volumes



Source: Savills

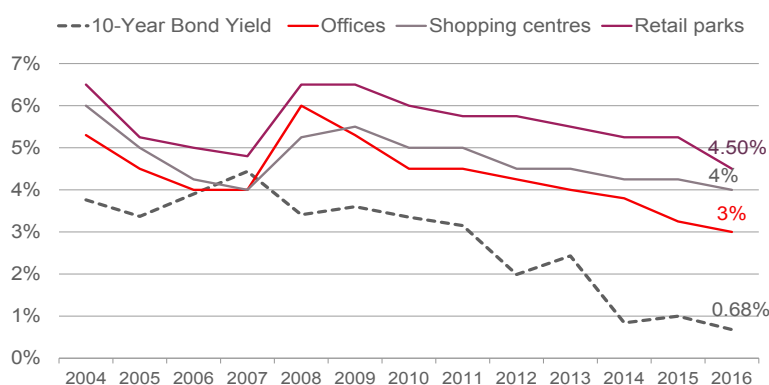
→ Rising profile of foreign investors

■ French investors still dominate their market (64% of total investments), however, some landmark deals in 2016 clearly highlighted the presence and interest being shown by foreign investors. One such deal was the debut

of the Koreans who completed three deals worth over €100 million each, and the Norwegians, with the acquisition of 9 Place Vendôme in Paris' 1st arrondissement for €1 billion. ■

GRAPH 2

Prime yields Increased uncertainty has failed to significantly impact markets



Graph source: Savills

OUTLOOK

Changing lay of the land for the market

■ 2017 is likely to see the return of inflation (>1%), primarily caused by higher commodity prices. The impact on interest rates should be limited though, given that growth is expected to be muted in 2017.

■ The French market is likely to become more attractive thanks to the Brexit effect, resulting from the relative lack of investor confidence, that is set to take hold until discussions between the UK and the EU member states are concluded.

■ The French market may also benefit from a return of German buyers in 2017. Having kept their distance in recent years, their portfolios are now under-invested in the French market and now would appear to be the time for readjustments.

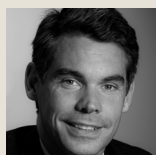
■ In light of all these factors, investment volume in 2017 should be in line with that of 2016, as long as there are no major political upheavals.

Savills France

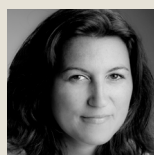
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